20 December 2019

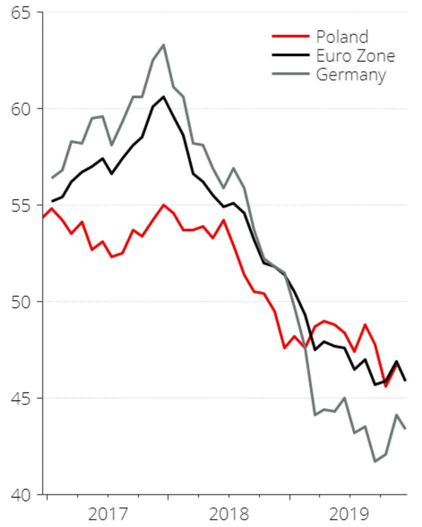
Bi-Weekly Economic Update

Merry Christmas and a Happy New Year!

What's hot in next two weeks

- The economy and financial markets are entering the holiday mode, investor activity and market liquidity may be reduced in the coming days. There is little in the local and global calendars for the next two weeks.
- On Monday there will be the last portion of domestic statistics before the end of the year, with construction output, which in our view will confirm a prolonged decline (-2.4% y/y), consistent with a stagnation in infrastructural investments (and burdened with negative working day difference). Statistical Bulletin will be also released, showing if the November drop of wage growth was due to delayed bonus payments in mining or a broader phenomenon.
- Just after the New Year, the focus will be on manufacturing PMIs. Flash readings for Europe showed a fall. We assume that the Polish index remained clearly below 50 pts, i.e. in the zone that signals declining economic activity.
- Apart from a few data releases we can also get some political news. Poland is again earning bad publicity due to the highly controversial changes in the judicial system proceeded in the parliament (the EC has already expressed its disapproval for a newly proposed draft bill on disciplinary measures against judges), but work on this issue may stop for a while as there are no more Sejm sittings planned this year. In the meantime, new information may be coming on the government plans to compensate electricity price hikes to households. Abroad, the issues to watch still include the Brexit developments, US-China trade talks and the impeachment procedure against Donald Trump (the House of Representatives passed the motion, but is delaying the moment it reaches the Senate).

Manufacturing PMIs



Source: Refinitiv Datastream

Market implications

- December is traditionally a month of stronger zloty. EURPLN may remain in the coming days slightly above 4.25 thanks to positive global sentiment, but its potential for further decline may be limited by local factors (weakness of the data, new controversies regarding the judiciary system).
- Bond yields rose in the recent days and if the core markets do not send any new signals, which would negate this trend, then we may see an extension of the move. Polish 10Y paper broke above the tight range it which it had stayed since the last days of November. After breaking 2.015% it can target 2.10%. It is important to note that the 10Y Bund yield breached the -0.218% resistance level (November peak). We believe that as the end of the year approaches, the volatility on the Polish market will be getting smaller.

Please be advised that today's Weekly Economic Update
will be the last for 2019.
We will resume publication on January 3, 2020.
We wish our readers Merry Christmas
and a prosperous New Year!

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What's hot next week

In November **industrial output** grew by 1.4% y/y vs market expectations at 0.3% and our 1.6% call. The SA result was also strong. The details showed a weak result of manufacturing and a large contribution from utilities. More in Economic comment.

In November, Polish **retail sales** rose by 5.2% y/y in real terms, beating the consensus of 3.9% and our 4.3% forecast. We attribute this positive surprise to the holiday season shopping activity, boosted by additional social transfers. More in Economic comment.

In December there was a further decline of **business sentiment** in Poland. The synthetic index dropped to 99.7 pts, below the 100-point long-term average for the first time in three years (indexes for industry and services fell, construction and retail trade rose).

In November Polish corporate **employment** rose by 2.6% y/y, a notch higher than expected and vs October. The m/m rise of 12k is actually quite high for November. The reading does not change our forecast of a slowdown in employment growth in 2020. **Wages** grew by only 5.3% y/y vs both expectations and the previous result at 5.9%. The implied real wage bill growth estimate, based on corporate sector data, was 5.3% y/y, the lowest in three years. In general, we think the annual average wage growth in the corporate sector will fall from c6.6% in 2019 to c6% in 2020 (of which around 1pp will come from the large hike of the minimum wage).

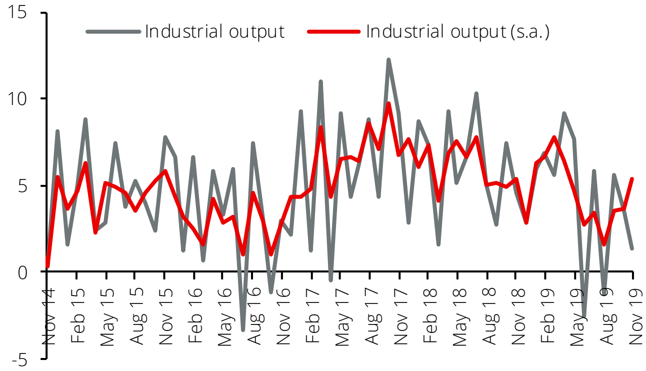
In December, **consumer confidence** indicators regarding current assessment and expectations became the lowest this year. The last time the joint two-month decline of economic situation expectations was as large as now was eight years ago. Unemployment worries also kept rising and are already the highest in three years. At the same time the gauge of openness to major purchases is still close to the record high from September.

Energy Regulatory Office (URE) approved the new **electricity price tariff** of Tauron Sprzedaż (supplying around 1/3 of Polish households) with the price of electricity rising by 20% which translates into 12% hike of electricity bill for the households (electricity bill includes also some other elements). Motions submitted by other electricity companies were rejected. Our earlier assumption of an average increase of energy price in 2020 of c10% looks pretty realistic. However, the effect of this rise could differ somewhat in terms of timing of the impact on CPI vs our initial assumptions – the remaining companies will not manage to correct their motions and have them approved in time to increase electricity prices already in January. URE announced also its decision regarding **gas price for households** – it approved a price cut by 2.9% which means the average bill could fall by 1.8%. This would only marginally offset the rise of electricity price in household budgets. The government is preparing a mitigating mechanism but might only cover low income households.

According to the December **MPC minutes**, there was another 25bp rate cut vote. We think the motion had no higher support this time than at the previous two meetings (1/10). The document shows that most of the members still think that rates should stay in place in the following quarters. The majority view is also that inflationary pressure is still moderate and that the issue of negative real interest rates is not worrying. We maintain the view that in 2020 and possibly 2021 there will be no rate changes in Poland. According to RMF FM radio station, **MPC's Jerzy Osiatyński will be replaced by Cezary Kochalski**, Poznan Economic University professor, expert in corporate finance; currently presidential advisor and president's envoy to the Financial Supervision Authority (KNF).

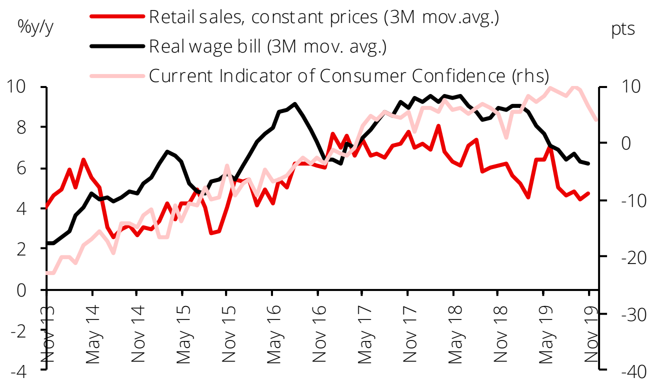
This week we released our **year-ahead report** "MACROscope – 2020 Outlook: Gear down to three" with the updated forecasts for the Polish GDP, inflation and exchange rates. Enjoy the reading.

Industrial production, %y/y



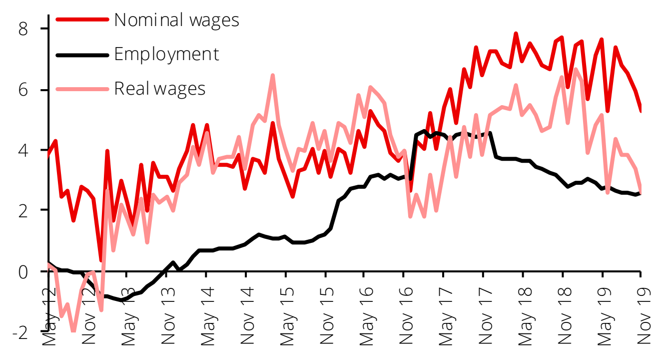
Source: GUS, Santander

Retail trade, consumer confidence and income



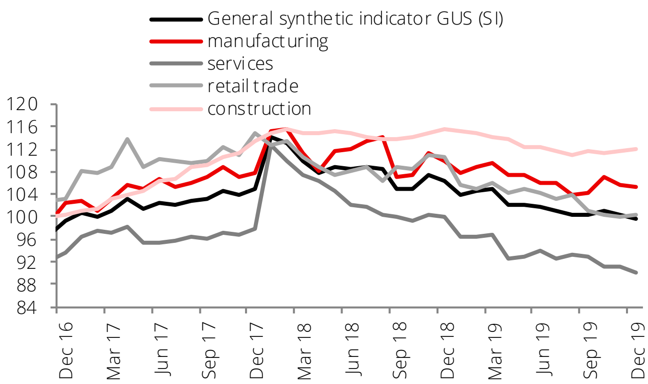
Source: GUS, Santander

Employment and wages in the corporate sector, %y/y



Source: GUS, Santander

Sectoral business sentiment measures



Source: GUS, Santander

FX and FI market

Last week on the market

FX Only in the first days of the passing week the zloty continued the appreciation momentum initiated by the positive news regarding the UK elections results and US-China trade deal. EURPLN neared 4.25, its lowest since early November as the main global stock indexes reached their fresh all-time/multi-month peaks. USDPLN reached 3.81, CHFPLN fell to 3.88 and GBPPLN traded below 5.0 but the zloty did not manage to keep initial gains. In general, EURPLN is so far holding the patter of a "traditional" December zloty appreciation.

In the CEE region, USDRUB remained stable around 62.5, EURCZK fell temporarily to 25.41 while EURHUF touched 328 before it rebounded back to 331.

FI On the domestic interest rate market volatility was low for the better part of the week and only in the second half we saw yields and IRS rising noticeably. Both curves steepened a bit while the asset swap spreads rose only marginally. On the core debt market, yields rose as well in response to decent US macro data.

Key events

The final two weeks of the year are expected to be rather quiet amid below-average liquidity.

Yet in 2020 we will see Polish construction output data and at the very beginning of the next year, manufacturing PMI will be released.

Abroad, the US data will dominated the calendar.

Market implications

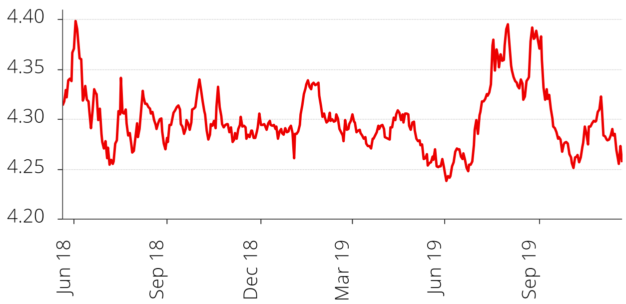
FX EURPLN has approached the 4.24-4.25 support area we expect will prevent the exchange rate from a further decline. Overall, the global market sentiment should remain rather positive although last week we have already seen some scratches. PM Boris Johnson said that he intends to introduce law that would eliminate the option of extending the transition period (that would start at the end of January 2020 if UK leaves the EU by then) beyond 2020. The outlook for a very short time to negotiate a new trade deal and other issues reminded that the risk of hard Brexit is not completely off the table.

In the short term, we would expect EURPLN to stay low slightly above 4.25 amid supportive global market mood but the room for a further decline looks to be limited also by some internal issues. Polish FX-mortgage loans case re-emerges on the wires from time to time and this could also keep zloty gains in check. Also, we anticipate more evidence that the domestic growth is slowing which will make the risk-factor balance change towards zloty-positive even less possible.

FI Polish bond yields are holding in a horizontal trend since September and since the beginning of the new year the two opposite forces may drive the market. On the one hand, two main risk factors (hard Brexit and intensification of the trade war) faded at least in the short term which would imply higher yields. Furthermore, global data start to show a shy attempts of improvement which should be debt-negative. On the other hand, however, Polish macro data are likely to show continuation of a gradual economic growth deceleration which could keep market expectations for a rate cuts alive.

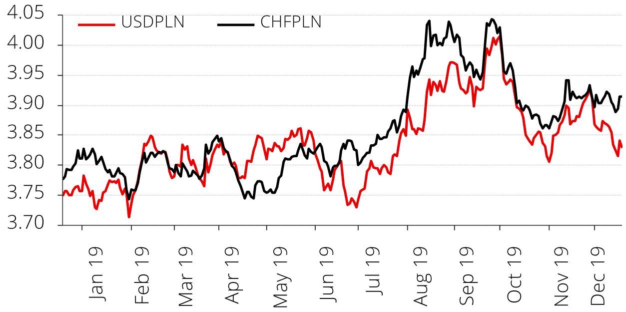
Polish 10Y bond yield left the narrow trading range in which it has been holding since late November. After breaking 2.015%% and the next target could be 2.10%. Note, that the 10Y Bund yield broke resistance at -0.218% (November peak). We assume that volatility on the Polish market could be falling since the year is coming to an end.

EURPLN



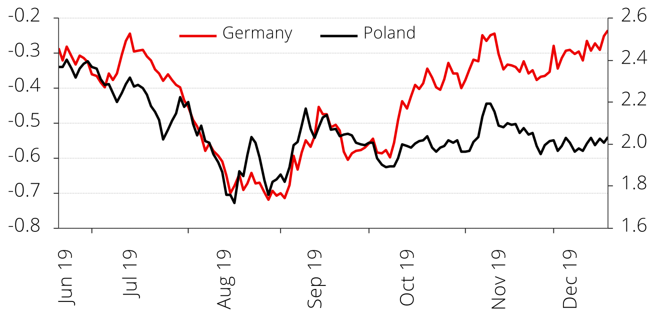
Source: Refinitiv Datastream, Santander Bank Polska

USDPLN and CHFPLN



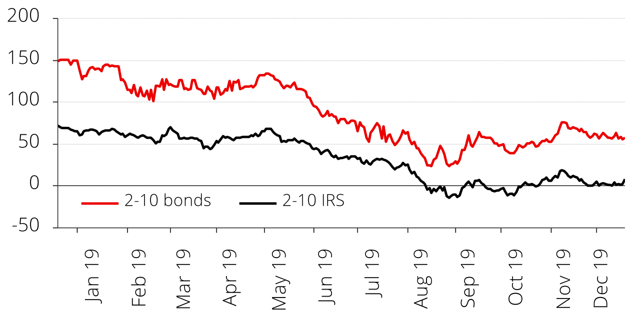
Source: Refinitiv Datastream, Santander Bank Polska

Poland and German 10Y bond yields



Source: Refinitiv Datastream, Santander Bank Polska

2-10 bond and IRS spreads



Source: Refinitiv Datastream, Santander Bank Polska

Economic Calendar

TIME CET	COUNTRY	INDICATOR	PERIOD		FORECAST MARKET	FORECAST SANTANDER	LAST VALUE
			MONDAY (23 December)				
10:00	**PL**	**Construction Output**	**Nov**	**% y/y**	**-6.4**	**-2.42**	**-4.0**
10:00	**PL**	**Unemployment Rate**	**Nov**	**%**	**5.1**	**5.1**	**5.0**
14:00	**PL**	**Money Supply M3**	**Nov**	**% y/y**	**9.15**	**9.36**	**9.3**
14:30	US	Durable Goods Orders	Nov	% m/m	1.5	-	0.5
16:00	US	New Home Sales	Nov	% m/m	-0.41	-	-0.7
			THURSDAY (26 December)				
14:30	US	Initial Jobless Claims	Dec.19	k	220	-	234
			FRIDAY (27 December)				
	DE	Retail Sales	Nov	% m/m	1.0	-	-1.6
			MONDAY (30 December)				
16:00	US	Pending Home Sales	Nov	% m/m	1.5	-	-1.7
			TUESDAY (31 December)				
16:00	US	Consumer Conference Board	Dec	pts	128.0	-	125.5
			THURSDAY (2 January)				
09:00	**PL**	**Poland Manufacturing PMI**	**Dec**	**pts**	**46.75**	**47.6**	**46.7**
09:55	DE	Germany Manufacturing PMI	Dec	pts	43.4	-	43.4
10:00	EZ	Eurozone Manufacturing PMI	Dec	pts	45.9	-	45.9
			FRIDAY (3 January)				
14:00	DE	HICP	Dec	% m/m	0.5	-	-0.8
16:00	US	ISM manufacturing	Dec	pts	49.0	-	48.1
20:00	US	FOMC Meeting Minutes	Dec.19				

Source: Santander Bank Polska, Reuters, Parkiet, Bloomberg

Additional information is available on request. Please contact Santander Bank Polska S.A. Financial Management Division. Economic Analysis Department. al. Jana Pawła II 17. 00-854 Warsaw. Poland. phone +48 22 534 18 87. email ekonomia@santander.pl. http://www.santander.pl.